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SITUATION REPORT

CHINA-VIETNAM-USSR

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25X1. The military and political situation generally remains static. [redacted]

25X1 Both sides continue to express confidence, and have been repeating well-worn political themes with little variation. The Soviets, for their part, continue to inveigh against the Chinese but still refrain from suggesting they will take specific, direct action in support of the Vietnamese. [redacted]

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Chinese-Vietnamese Political Activities

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//Chinese officials and diplomats remain remarkably upbeat in their assessment of the border situation and the possibility of serious Soviet intervention. On Wednesday, Vice Premier Geng Biao told a visiting Swedish official [redacted] that Chinese forces would remain in Vietnam for another week or "perhaps a little bit longer," and Vice Foreign Minister Zhang Wenjin told a West German diplomat that China alone would determine when a withdrawal would be undertaken. Zhang stated that the USSR could only mount a small-scale attack on China within the time period the Chinese will remain on Vietnamese soil.//

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Zhang also claimed that China's problems with Vietnam are purely bilateral. He indicated that if the border situation were raised in the UN Security Council, China would insist that it be treated separately from the Vietnamese invasion of Kampuchea and only after that issue were resolved. Earlier in the week, the Chinese Ambassador to the UN was telling some missions that if they would delay calling for a Security Council meeting, China might have "something new" to say on Thursday about the border situation. Beijing, however, made no new statements yesterday. [redacted]

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Asian Reaction

Public and private statements by Japanese Government leaders have called on all parties to the conflict in Indochina, including the Soviet Union, to exercise

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restraint and work toward an end to hostilities in the region. According to the Japanese Foreign Ministry, Ambassador Sato requested of Foreign Minister Huang Hua in Beijing on Monday that China withdraw its forces from Vietnam. The Japanese reportedly plan a parallel representation in Hanoi calling for a Vietnamese withdrawal from Cambodia. Depending on events in the next few days, Japan is apparently considering underscoring the counsel of restraint already given Soviet Ambassador Polyansky in Tokyo by Prime Minister Ohira. Japanese Foreign Ministry officials, meanwhile, have privately said that Tokyo will support the US initiative to convene the UN Security Council to address both the Sino-Vietnamese conflict and the situation in Kampuchea. [redacted]

Other Reaction

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//The UK yesterday announced the suspension of talks with China concerning the sale of Harrier aircraft. A British spokesman declared that the time was inappropriate for the negotiations, adding that if China is involved in a large-scale war in Vietnam, Britain could not supply the aircraft.// [redacted]

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Soviet Political Reaction

//Most private and public Soviet comment continues to suggest that--for now at least--the Soviets are confident of Vietnam's ability to handle the Chinese without the need for direct Soviet military involvement. When queried as how the USSR will fulfill its treaty commitment to Vietnam, Soviet officials continue to raise the possibility of increased aid and advisers, perhaps even "volunteer" pilots, but they specifically rule out any Soviet action along the Sino-Soviet border or the commitment of Soviet military units to Vietnam. The US Embassy in Moscow notes that in its contacts with mid-level officials at the Foreign Ministry and various academic institutes, Soviet officials do not appear to foresee the need for direct Soviet involvement both because China's action is expected to be limited and because the Vietnamese seem to be holding their own.// [redacted]

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Soviet leaders, however, continue their attempt to put Washington on the defensive by claiming to see a US tilt toward China in the present crisis. KGB Chairman

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Andropov and Leningrad party boss Romanov yesterday became the third and fourth Politburo members to condemn the Chinese invasion, and both hinted at--but did not directly charge--US complicity in the invasion. Andropov said that a policy of attempting to use China against the USSR is incompatible with strengthening detente and building up confidence among nations, and Romanov condemned those who offer "direct or indirect justification for Beijing's course."

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We have no evidence to support Japanese newspaper reports that the USSR has begun mobilizing troops along the Chinese border and in Mongolia.

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BRIEFS AND COMMENTS

FRANCE: Possible Export Curbs on Oil Products

A French official strongly implied to a US Embassy officer in Paris that France intends to impose export quotas on oil products if the domestic supply situation continues to worsen. Such action would most likely be directed against France's EC partners, particularly West Germany, and would be in clear violation of EC rules.

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French refiners reportedly are favoring sales to West Germany at the expense of the home market. The French Government maintains a price control program for oil products and has not allowed domestic retail rates to rise enough to compensate for increases in the spot price of crude oil in European ports. West Germany, on the other hand, is allowing prices to climb. Imports of French oil products account for 2 to 3 percent of total West German oil consumption.

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The French Government recently implemented an export licensing system for petroleum products. The system was described as an information-gathering device, but it would help the government quickly establish export quotas.

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At recent cabinet meetings, the government decided to raise heating oil prices but kept gasoline prices constant to avoid further inflationary effects. It has made no decision yet whether to dip into France's strategic oil reserves. The French official stated that if Iranian oil shortfalls continued the government eventually would be forced to allow retail prices to climb to levels that would encourage refiners to produce for the domestic market. President Giscard has called for international energy cooperation and will raise the matter next month at the meeting of EC heads of state.

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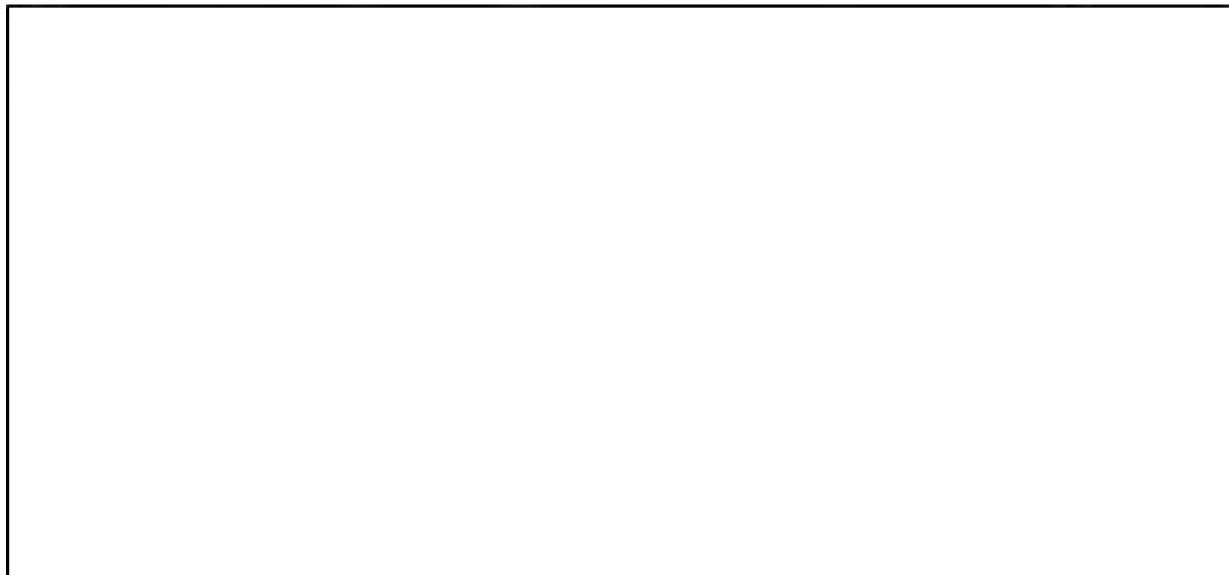
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USSR-BULGARIA: Possible Exercise

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//The Soviets and Bulgarians are reportedly planning to hold a joint exercise in Bulgaria next month. [redacted]

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[redacted] If an exercise is held, it is likely to be a command and staff exercise involving few personnel and little tactical play. Last March, the USSR, Romania, and Bulgaria held such an exercise in Romania. The cooling of relations between the Soviets and Romanians since then may preclude Romania's participation this year. Yugoslavia probably would see such an exercise as indirect Soviet pressure resulting from sharpening differences on foreign policy issues.// [redacted]

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ECUADOR: Military Court to Try Jarrin

//Former Government Minister General Bolivar Jarrin will be tried by a military court for complicity in the assassination of national political leader Abdon Calderon last November. Jarrin was dropped from the cabinet the following month when it was learned that Calderon was killed by political thugs working for the Government Ministry. By trying Jarrin in a military rather than a civilian court--where his codefendants have been arraigned--the government probably is seeking both to protect the reputation of the military and to minimize the possibility that Jarrin will implicate other government leaders. Because of such considerations, the military proceedings could be held in camera.//

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SPECIAL ANALYSIS

SAUDI ARABIA: More Moderate Development Pace

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Last year's cash flow crisis, coupled with the Iranian upheaval, probably has convinced Saudi leaders that they must slow the pace of economic expansion. For more than a year, unsettling experiences with inflation and the influx of foreign labor have led a substantial group in the Saudi hierarchy to question the wisdom of forced-draft modernization. The Saudis' cautious statements concerning the next phase of their development plan have suggested that future plans for growth will be more conservative.

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Saudi Arabia first attempted to accelerate development with its First Development Plan (FY 1971-75). The sharp rise in oil prices in 1973 and 1974 caused budget allocations during the latter years of the plan to be expanded far beyond original targets. The Second Development Plan (FY 1976-80) was aimed at continuing rapid growth through diversification of the economy's productive base, training, expansion of social benefits, and development of roads, ports, and other supporting facilities. Even though budget allocations were not fully spent, the upsurge in actual government outlays led to a boom atmosphere with rapidly rising wages and prices.

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By 1976, officials were beginning to realize that physical and social bottlenecks limited the speed at which government could promote growth and that any program exceeding the absorptive capacity of the economy would cause inflation, shortages, and project delays. Fiscal policy thus was tightened through stricter spending controls and postponement or stretching out of some development projects.

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The only area in which spending has consistently exceeded allocations has been in transfers, subsidies, and foreign aid. This category includes subsidies to low-income groups and universities and to domestic

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credit institutions that provide concessionary financing in real estate, service enterprises, agriculture, and industrial development. These latter transfers have encouraged private sector participation in the development process. [redacted]

The Saudis learned their most traumatic lesson in mid-1978 as a result of haphazard budgeting procedures. Ministries notoriously failed to coordinate plans, and oil revenues were sometimes calculated in ignorance of the government's oil policy. Under these conditions, the initial FY 1979 budget draft grossly underestimated ministry funding requests and overestimated oil revenues, necessitating an across-the-board slash in total requests followed by a 33-percent cut in project funding. [redacted]

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Reduced oil production, rising imports, and loss of purchasing power due to the decline of the dollar, forced the Saudis several times during 1978 to cash in maturing investments and to draw down reserves in September. The disruption of development was small, however, because the desire to keep projects going outweighed an initial reluctance to draw on foreign assets. [redacted]

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Saudi achievements under the Second Plan are falling far short of the original targets. There have been substantial achievements nevertheless. Progress has been particularly notable in eliminating import bottlenecks through port development, in creating educational institutions, and in extending medical care. The government is sharing the fruits of development with native Saudis, and low-income groups are benefiting from social security payments, food subsidies, and rent controls. Any citizen with initiative has access to low-cost credit for industrial, commercial, and agricultural ventures. Entrepreneurs have taken advantage of these conditions to develop real estate businesses, to enter franchise arrangements with foreign partners, and to establish businesses involving the transportation or marketing of imported goods. [redacted]

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So far, however, few Saudis have invested in heavy industry, and government programs in this sector are moving slowly. Most of the government-sponsored industrial projects to be located at Jubayl on the Persian Gulf coast and Yanbu on the Red Sea are still in the

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planning and preparation stage. A gas-gathering system and some cross-country pipelines are the only industrial facilities actually under construction, and these are running at least three years behind original schedules. An aluminum smelter and a steel plant may have been deferred indefinitely; the Saudis have not yet decided when to proceed on two fertilizer and two cement plants needed to push development in the nonoil sector. Petrochemical projects, mainly involving US corporations, are being delayed by the tortuous process of Saudi decision-making.

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Saudi disenchantment with the cost and direction of the development process is evident in several major respects, and the government is moving to make important changes. Under various guises, previously negotiated contracts have been called in for renegotiation, leading to a claimed 30-percent saving over original contract costs. Leading officials are also concerned about industrialization schemes that profit from government loans and protection but do not integrate Saudis into management and do not train Saudis for skilled jobs.

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The next Saudi development plan presumably will stress expansion of productive industry, increased private participation in industry, the maintenance of traditional social values, and development of managerial and technical skills by native Saudis.

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